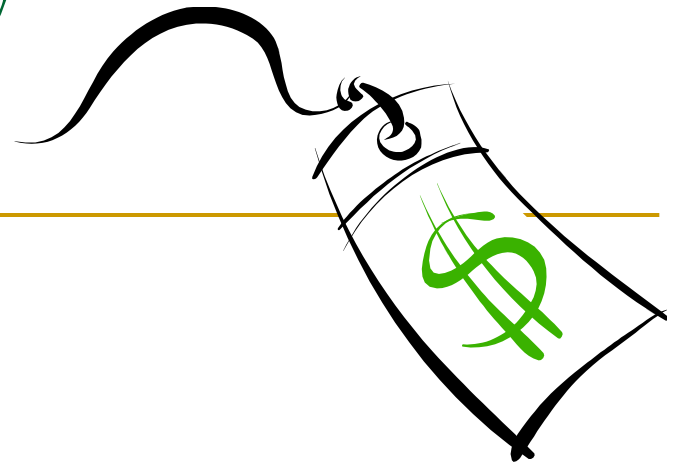

Chapter 11

The Price Strategy

Business Ownership
Mrs. Deady



Objectives

- Identify factors that affect price strategy
 - Explain the marketing objectives related to pricing
 - Describe the components that go into making price strategy decisions
 - Carry out a break-even analysis
 - Apply formulas used in calculating markup and markup percentages
 - Use markdown formulas to determine sale price
 - Employ formulas used to compute discounts
 - Lost considerations for updating the price strategy
-

Definitions 11.1

Considering Price Strategy

- Fixed – costs and expenses not subject to change based on number of units sold
 - Variable – costs and expenses that change based on number of units sold
 - Price gouging – pricing above market when no alternative retailer is available
 - Price fixing – illegal – competing companies agree to restrict prices within a specified range
 - Resale price maintenance – price fixing imposed by a manufacturer on wholesale or retail resellers of its products to deter price-based competition.
 - Unit pricing – required pricing of goods on basis of cost per unit of measure (by pound) in addition to price per item
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Definitions 11.1

Considering Price Strategy, cont'd

- Bait-and-switch – advertising method to attract buyers only to find it out of stock or inferior to higher-priced item that is available.
- Return on investment – ROI – amount earned as a result of that investment
- Price skimming – charging a high price to recover costs and maximize profit quickly
- Penetration pricing – charging a low initial price to attract sales (and discourage competition)
- Psychological pricing – belief that customers' perceptions of a product are strongly influenced by price
- Prestige pricing – higher-than-average price suggests status and prestige; associated with higher quality

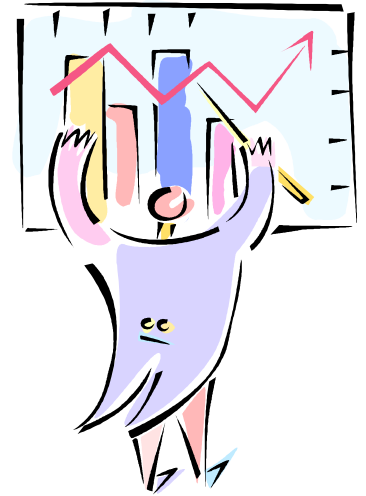
Definitions 11.1

Considering Price Strategy

- Odd/even pricing – odd numbers suggest bargains; even numbers suggest higher quality
 - Price lining – low, middle and high pricing for different categories of goods
 - Promotional pricing – lower prices offered for a limited time to stimulate sales
 - Multiple-unit pricing – items priced in multiples, 3 for 99 cents, suggests a bargain
 - Bundle pricing – several complementary products sold at a lower price than if purchased separately
 - Discount pricing – offers customers reductions (cash, quantity, trade, promotional, seasonal)
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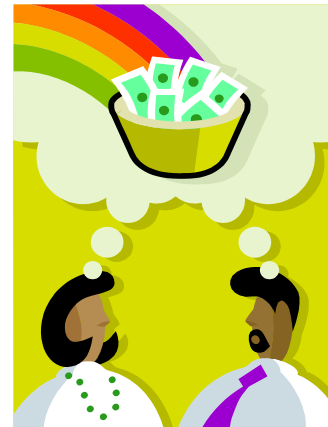
What Factors Affect Price???

- Costs and Expenses
- Supply and Demand
- Consumer perceptions
- Competition
- Government Regulations
- Technological trends



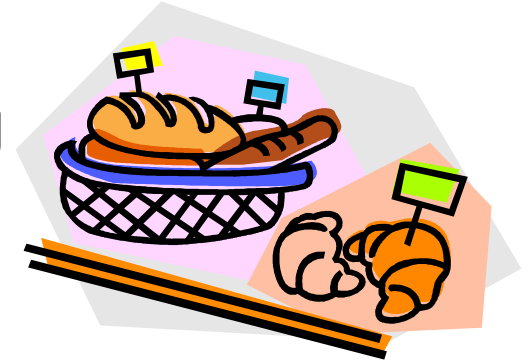
What are the Important Pricing Objectives?

- To obtain a targeted Return on Investment. The product should be priced to earn an expected profit.
- To obtain Market Share
- Social and Ethical Considerations
- Survival



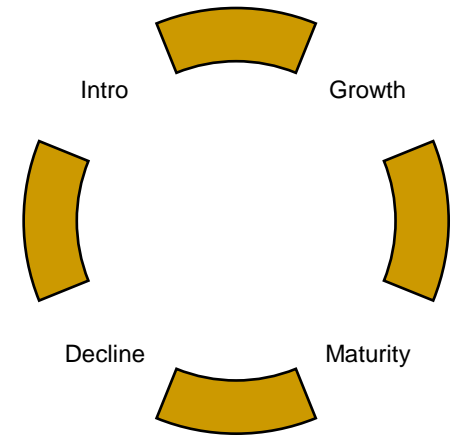
How do you set a Basic Price?

- Select a basic approach to pricing
 - cost-based: price = cost plus markup
 - demand-based: what customers are willing to spend
 - competition-based: be below, in-line or above competition
- Determine your pricing policy
 - flexible-price – like car dealerships
 - one-price – all customers treated equally
- Set a price based on the stage of the product life cycle (introduction, growth, maturity or decline) using an effective pricing technique (psychological pricing or discount pricing).



Product Life Cycle Pricing

- Stage 1 – Introduction: since costs are high and profits low, use price skimming to recover costs and maximize profit OR penetration pricing to build sales
- Stage 2 – Growth: If you used price skimming, lower prices to appeal to price-conscious customers; if you used penetration pricing, make only minor price changes – use other promotions to increase sales.
- Stage 3 – Maturity: Sales begin to slow down, so you need to identify new markets or make product improvements to extend the maturity stage.
- Stage 4 – Decline: As sales and profits continue to fall, cut prices to generate sales or clear inventory; phase out the product.



Psychological Pricing Techniques

- Psychological pricing is the belief that customers' perceptions of a product are strongly influenced by price. Included are:
 - Prestige pricing – higher-than-average price suggests status and prestige; associated with higher quality
 - Odd/even pricing – odd numbers suggest bargains; even numbers suggest higher quality
 - Price lining – low, middle and high pricing for different categories of goods
 - Promotional pricing – lower prices offered for a limited time to stimulate sales
 - Multiple-unit pricing – items priced in multiples, 3 for 99 cents, suggests a bargain
 - Bundle pricing – several complementary products sold at a lower price than if purchased separately
-

Discount Pricing



- Reductions from the regular price encourage customers to buy. They are given through:
 - ❑ Cash Discounts for prompt payment (reduce bill by 2% for paying within 10 days)
 - ❑ Quantity Discounts – reduce price by buying more; reduce shipping; make buyer responsible for financing; be cumulative over the course of a year can be given a 10% discount
 - ❑ Trade Discounts – given to distribution-channel members
 - ❑ Promotional Discounts – to pay wholesalers or retailers for carrying out promotional activities
 - ❑ Seasonal Discounts – to customers who buy in off-season
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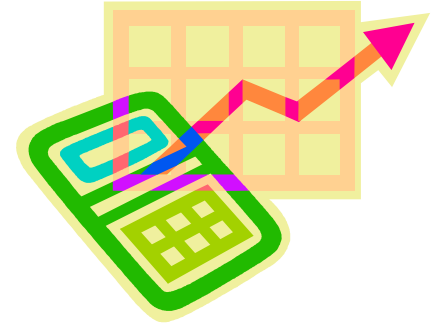
Definitions 11.2

Calculating and Revising Prices



- Break-even point – sales equal the costs and expenses of making or distributing a product
- Selling price – actual or projected price per unit
- Markup – amount added to the cost of an item to cover expenses and ensure a profit
- Markdown – amount of money taken from the original price

Calculations and Formulas



Breakeven is equal to:

- $\frac{\text{Fixed cost}}{\text{Unit selling price} - \text{variable costs}} = \text{Break-even point (units)}$

Markup is equal to:

- $\frac{\text{Markup}}{\text{Cost}} = \text{Percentage Markup on Cost}$
 $\text{Price} - \text{Markup} = \text{Cost}$

Markdown is equal to:

- $\text{Price} \times \text{Markdown\%} = \$ \text{ Markdown}; \text{ then}$
 $\text{Price} - \$ \text{ Markdown} = \text{Sale Price}$

How to Maximize Profit

You need to consider:

- ❑ Are your products' prices elastic or inelastic?
- ❑ What are your competitors' prices?

